

Department of Legislative Services
 Maryland General Assembly
 2013 Session

FISCAL AND POLICY NOTE

House Bill 683 (Delegate Luedtke, *et al.*)
 Ways and Means and Health and
 Government Operations

Tobacco Taxes - Healthy Maryland Initiative

This bill increases the tobacco tax rate from \$2.00 to \$3.00 per pack and the other tobacco product (OTP) tax rate from 30% to 95% of the wholesale price except for certain cigars. In addition, the bill mandates specified minimum and maximum tax rates for certain other tobacco products. OTP tax revenue is redistributed from the general fund to a special fund to ensure that tobacco cessation programs receive at least \$21 million in annual funding beginning in fiscal 2015. Any additional money in the special fund is to be used to support specified health care programs.

The bill takes effect July 1, 2013, except for provisions related to an OTP tax fund that take effect July 1, 2014.

Fiscal Summary

State Effect: Net general fund revenues increase by \$36.7 million in FY 2014 due to the increase in the cigarette tax, minus the loss of sales tax and OTP revenues. Special fund OTP tax revenues increase by \$44.8 million in FY 2014; OTP special fund expenditures increase by a corresponding amount for specified health care programs. Future year estimates reflect estimated OTP and cigarette tax revenues and OTP special fund expenditures specified by the bill.

(\$ in millions)	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
GF Revenue	\$36.7	\$33.6	\$30.8	\$27.7	\$24.5
SF Revenue	\$44.8	\$46.2	\$47.5	\$48.9	\$50.5
SF Expenditure	\$44.8	\$46.2	\$47.5	\$48.9	\$50.5
Net Effect	\$36.7	\$33.6	\$30.8	\$27.7	\$24.5

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: None.

Small Business Effect: Meaningful.

Analysis

Bill Summary: The bill increases the tobacco tax rate from \$2.00 to \$3.00 per pack and the OTP tax rate from 30% to 95% of the wholesale price except for certain cigars. In addition, the bill provides specified minimum and maximum tax rates for certain other tobacco products. The tax rate on other tobacco products is equal to:

- 95% of the wholesale price for cigars, not to exceed \$3.00 per cigar for cigars with a wholesale price of less than \$20.00, or 15% of the wholesale price for cigars with a wholesale price of \$20.00 or greater.
- the greater of 95% of the wholesale price or (1) \$3.00 per 1.2 ounce container of moist snuff tobacco; (2) 15 cents per dose of single dose smokeless tobacco; and (3) \$3.00 per 0.65 ounces of roll-your-own tobacco.

In addition, small-cigar cigarettes are taxed at the same rate as cigarettes. A small-cigar cigarette is defined as a small, thin cigar with the approximate dimensions of a cigarette or a cigarette wrapped in tobacco instead of paper.

The bill requires the Comptroller's Office to distribute OTP tax revenues to an OTP tax fund created by the bill. The fund may be used to provide additional funding for the State Tobacco Use Prevention and Cessation Program and to ensure that the program receives at least \$21 million in annual funding beginning in fiscal 2015. Any additional revenue remaining in the fund must be used to fund the State Health Improvement Process and other community-based health initiatives, including those that address childhood obesity, long-term care for seniors, and improved access to health care services for Marylanders. The bill also directs \$10.8 million of the tobacco tax revenues generated from the bill in fiscal 2014 to the Tobacco Use Prevention and Cessation Program.

Any money expended from the fund to support the Tobacco Use Prevention and Cessation Program and health care programs described above is supplemental to and is not intended to take the place of funding that otherwise would be appropriated for those purposes.

Current Law: Cigarettes are taxed at a rate of \$2.00 per pack. OTP are taxed at 30% of the wholesale price for all products, except cigars. The tax rate for cigars that are classified as premium cigars equals 15% of the wholesale price; all other cigars are taxed

at 70% of the wholesale price. Cigarette and OTP tax revenues accrue to the general fund. In addition, the State sales tax rate of 6% is imposed on the final retail price of cigarettes and other tobacco products.

Background: Chapter 121 of 1999 (HB 190) increased the cigarette tax from 36 cents to 66 cents. In addition, Chapter 121 imposed a 15% tax on the wholesale price of OTP such as cigars and smokeless tobacco. Chapter 288 of 2002 (SB 856) increased the cigarette tax from 66 cents to \$1.00 per pack. Chapter 6 of the 2007 special session (HB 5) increased the cigarette tax to \$2.00 per pack. In fiscal 2010, of the total amount of OTP reported sold by wholesalers, 63% was cigars, followed by moist snuff (25%), chewing tobacco (7%), roll-your-own tobacco (4%), and pipe tobacco (1%).

Chapter 2 of the first special session of 2012 (SB 1302) increased the OTP tax rate from 15% to 30% of the wholesale price for all products except cigars effective July 1, 2012. The tax rate for cigars that are classified as premium cigars remained at 15% of the wholesale price; all other cigars are taxed at 70% of the wholesale price.

The Tobacco Use Prevention and Cessation Program aims to reduce the use of tobacco products and to reduce the burden of tobacco-related morbidity and mortality in the State. Over the past several years, the State's fiscal difficulties have prompted reductions to the mandated funding levels for various programs funded by the Cigarette Restitution Fund. The Budget Reconciliation and Financing Act of 2010 (Chapter 484/SB 141) reduced annual appropriations for tobacco use prevention and cessation activities to \$6 million in each of fiscal 2011 and 2012 and \$10 million annually beginning in fiscal 2013. Prior to these reductions, \$21.0 million was mandated for the activities annually.

The proposed fiscal 2014 State budget includes \$10.2 million in funding for the program.

Exhibit 1 shows the cigarette and OTP tax rates imposed in surrounding states as of January 1, 2013, and the tax rate for moist snuff tobacco in those states that provide for a separate tax.

Exhibit 1
Cigarette, OTP, and Moist Snuff Tobacco Tax Rates in Surrounding States

<u>State</u>	<u>Cigarette Tax Rate</u>	<u>OTP Tax Rate</u>	<u>Moist Snuff Tobacco (per Ounce)</u>
Delaware	\$1.60	15%	\$0.54
District of Columbia	2.50	12% *	0.75
Maryland	2.00	30% **	
Pennsylvania	1.60	None	
Virginia	0.30 ***	10% ****	0.18
West Virginia	0.55	7%	

* Applied to retail price of certain products.

** Tax rate on premium cigars is 15% of the wholesale price and 70% of the wholesale price for all other cigars.

*** Counties may impose an additional tax on cigarettes of \$0.02 to \$0.15

**** Applied to manufacturing price, chewing tobacco taxed per unit.

Source: Federation of Tax Administrators

State Fiscal Effect: The bill increases the cigarette and OTP tax rates and redirects OTP tax revenues to support tobacco cessation programs and specified health care programs. As a result, net general fund revenues increase by \$36.7 million in fiscal 2014 as shown in **Exhibit 2**. OTP special fund revenues increase by \$44.8 million in fiscal 2014.

OTP special fund expenditures increase by \$44.8 million in fiscal 2014. The bill mandates that revenues from the OTP tax ensure a total of \$21.0 million in annual tobacco cessation program funding beginning in fiscal 2015 and also support health care spending as specified by the bill. In addition, the bill requires a general fund appropriation of \$10.8 million in fiscal 2014 for tobacco cessation program funding.

The revenue estimates are based on past cigarette tax increases in Maryland and an examination of the additional OTP revenues generated through tax increases in 11 other states in fiscal 2006 through 2010, adjusted for Maryland. Based on these experiences, the estimates assume a significant reduction in the taxable consumption of cigarettes and OTPs following the tax increases.

Exhibit 2
Fiscal Impact of Legislation
Fiscal 2014-2018
(\$ in Thousands)

	<u>FY 2014</u>	<u>FY 2015</u>	<u>FY 2016</u>	<u>FY 2017</u>	<u>FY 2018</u>
Revenues					
<i>General Fund</i>					
OTP Revenues	(\$35,875)	(\$36,951)	(\$38,060)	(\$39,202)	(\$40,378)
Cigarette Tax	77,802	76,662	75,434	74,087	72,609
Sales Tax	(5,206)	(6,115)	(6,617)	(7,150)	(7,717)
Net General Fund	\$36,721	\$33,596	\$30,757	\$27,736	\$24,514
<i>Special Fund</i>					
OTP Revenue	44,833	46,164	47,535	48,947	50,472
Total Revenues	\$81,554	\$79,761	\$78,292	\$76,682	\$74,986
Expenditures					
Tobacco Cessation	10,800	11,000	11,000	11,000	11,000
Health Care Programs	34,033	35,164	36,535	37,947	39,472
Total Expenditures	44,833	46,164	47,535	48,947	50,472
Net Impact	\$36,721	\$33,596	\$30,757	\$27,736	\$24,514

Small Business Impact: Small businesses that sell cigarettes and other tobacco products will be negatively impacted due to the decrease in the sales of these products resulting from the tax increases.

Additional Information

Prior Introductions: Similar legislation was introduced in the 2011 and 2012 sessions. SB 526 of 2012 received a hearing in the Senate Budget and Taxation Committee, but no further action was taken. Its cross file, HB 1153 of 2012, received a hearing in the House Ways and Means Committee, but no further action was taken. SB 654 of 2011 received

an unfavorable report from the Senate Budget and Taxation Committee. Its cross file, HB 853 of 2011, received a hearing in the House Ways and Means Committee, but no further action was taken.

Cross File: SB 700 (Senator Jones-Rodwell, *et al.*) - Budget and Taxation and Finance.

Information Source(s): Department of Health and Mental Hygiene, Comptroller's Office, Federation of Tax Administrators, Department of Legislative Services

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mlm/jrb

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